Global Credit Card Industry: Issues and Challenges

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Abstract:
A credit card has blessed and facilitated the middle class with the power to chase and often purchase their dreams, which are generally beyond their means. Credit card is the substitution of the currency at a time when the transaction of buying and selling takes place. One of the main reasons for this kind of substitution is the postponement of payment i.e. cash. The credit card companies have also expanded quickly into the global market in order to exploit the opportunities that are provided by the emerging economies. The emerging economies will be the primary drivers of credit card revenue. The revenues from global credit card issuing will increase from $328 billion in 2011 to $445 billion in 2016. The United States and Brazil are the largest of these by revenue, accounting for more than half of global revenues despite the economic crisis; credit card revenue has continued to increase. This is largely due to growth in Brazil, China and other emerging markets. In this backdrop, an attempt is made to study the global credit cards issuing revenue and issues and challenges associated with global credit cards industry. Incidentally, this paper also analyses the future trends of global credit card industry.

Keywords: Credit Cards, revenue, payment.

Introduction:
Credit cards offer consumers and businesses short-term lines of credit and a variety of repayment options. Having a line of credit gives consumers the ability to cover unexpected or large expenses as well as make basic everyday purchases, and it helps consumers establish credit histories. The credit card companies have also expanded quickly into the global market in order to exploit the opportunities that are provided by the emerging markets. Credit card usage pattern of emerging markets differs from those of well-developed markets in important ways.
The factors that affect credit card usage pattern of consumers in emerging markets and the implications of these factors for developing marketing strategies may not be the same as those for well-developed markets. Understanding the factors that explain consumer behaviour of credit card users in emerging markets could provide an essential insight to marketing strategists of financial services, retailers, and businesses in promoting use of credit cards. The consumer credit card market is reaching the saturation point, so the industry needs to develop marketing strategies that appeal to changing customer needs in order to encourage credit card usage.
Formation of the Credit Card Industry:
Although merchant credit may be as old as civilization, the present-day credit card industry in the United States originated in the nineteenth century. In the early 1800s, merchants and financial intermediaries provided credit for agricultural and durable goods, and by the early 1900s, major U.S. hotels and department stores issued paper identification cards to their most valued customers. When a customer presented such a card to a clerk at the issuing establishment, the customer’s creditworthiness and status were instantly established. The cards enabled merchants to cement the loyalty of their top customers, and the cardholders benefited by being able to obtain goods and services using pre-established lines of credit. Generally these cards were useful only at one location or within a limited geographical area—an area where local merchants accepted competitors’ cards as proof of a customer’s creditworthiness.

In 1949, Diners Club established the first general purpose charge card, enabling its cardholders to purchase goods and services from many different merchants in what soon became a nationwide network. The Diners Club card was meant for high-end customers and was designed to be used for entertainment and travel expenses. Diners Club charged merchants who accepted the card 7 percent of each transaction. Merchants found that accepting Diners Club cards brought more customers who spent more freely. The Diners Club program proved successful, and in the following decade it spawned many imitators.

In 1966, in the wake of Bank of America’s success, a competing network of banks issued a rival card was established. This effort evolved over time into what is now the MasterCard network. In addition, firms that were not constrained by interstate banking restrictions formed card networks on the single-issuer model (the model established by Diners Club, in which many merchants accept payments on a card with a single issuer). For instance, the American Express Company (American Express) introduced its charge card system in 1958, and Sears,
Roebuck and Co. (Sears) established the Discover Card credit card in 1986. Among the challenges each of these networks faced was bringing together large numbers of cardholders with large numbers of merchants who accepted the cards as payment. Achieving a sufficiently large network was hard, partly because merchants, especially larger retailers, were reluctant to honor credit cards that would compete with their own store-branded credit cards. Some smaller merchants, however, viewed general-purpose credit cards as a way they could compete with larger merchants for customers. Merchants of all sizes were averse to having fees imposed on them by the credit card network. Credit cards were also widely accepted by merchants, and with the recent addition of fast food and convenience stores to the credit card networks, credit card payments are now processed at nearly all retail establishments.

Need for the Study:
Despite the ongoing economic crisis, cards transaction volumes globally have been increasing mainly due to strong growth in Asia Pacific, Latin America, and other emerging markets. Card transaction volumes are expected to continue to grow, with Brazil, China and other Asia Pacific regions being the main contributors. The average transaction value, however, is declining due to the geographic expansion of cards into emerging countries, and tapping into a low value segment i.e. —competing with cash, in mature economies. Hence, there is need to study the global credit card industry revenue and its issues and challenges.

Objectives of the Study:
The following are the main objectives of the study:

1) To examine the global credit cards issuing revenue
2) To study the issues and challenges associated with global credit card industry.
3) To present the future trends of global credit card industry

Source of Data:
The study is based on the data collected from secondary sources, gathered from the Annual Reports of different banks, published materials in the form of books, articles from journals, websites and reports relevant to the study. The study of global credit cards industry covers a period of 05-years, commencing from 31st March, 2005 to 2011.

Global Credit Card Issuing Revenues:
In 2011, global payments revenues accounted for 33 percent of total banking revenues. This figure is impressive, but perhaps a bit misleading, since more than 60 percent of global payments revenue derives from interest revenue, including current account deposits (59 percent), overdraft lines (16 percent) and credit card revolving loans (22 percent). In this, the10 nations account for more than 80% of global credit card issuing revenues. The relevant data collected and presented in Table – 1.

Table-1: Global Credit Card Issuing Revenues

<table>
<thead>
<tr>
<th>Sl. No</th>
<th>Top Ten Countries</th>
<th>Share of Total Revenue (US. $ Billions)</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>U.S</td>
<td>139</td>
<td>43%</td>
</tr>
<tr>
<td>2</td>
<td>Brazil</td>
<td>46</td>
<td>14%</td>
</tr>
<tr>
<td>3</td>
<td>Japan</td>
<td>26</td>
<td>8%</td>
</tr>
<tr>
<td>4</td>
<td>Canada</td>
<td>15</td>
<td>4%</td>
</tr>
</tbody>
</table>
Growth of Credit Card Revenue:
The growth of credit card revenue mainly depends on the fee and interest collected on credit cards usage. As interest rates face continued volatility, growth in revenue is expected to be driven by fee, rather than interest income. The credit card revenue through fee and interest data is collected tabulated and presented in Table-2.

Table -2: Growth of Credit Card Revenue (US. $ Billions)

<table>
<thead>
<tr>
<th>Years</th>
<th>Revenue based on Credit Card Fee</th>
<th>Revenue based on Credit Card Interest</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005-2006</td>
<td>114</td>
<td>138</td>
</tr>
<tr>
<td>2006-2007</td>
<td>125</td>
<td>148</td>
</tr>
<tr>
<td>2007-2008</td>
<td>134</td>
<td>166</td>
</tr>
<tr>
<td>2008-2009</td>
<td>126</td>
<td>198</td>
</tr>
<tr>
<td>2009-2010</td>
<td>130</td>
<td>196</td>
</tr>
<tr>
<td>2010-2011</td>
<td>138</td>
<td>190</td>
</tr>
<tr>
<td>2015-2016E</td>
<td>207</td>
<td>238</td>
</tr>
</tbody>
</table>

Source: McKinsey Global Payments Map

The above data reveals that the credit card fee revenues will increase faster than credit card interest revenue. While fees are expected to grow at a Compound Annual Growth Rate (CAGR) of 9 percent between 2011 and 2016, we may expect that interest income will increase at a CAGR of 5 percent in the same period. Whereas fees accounted for 42 percent of the global credit card issuing revenues in 2011, they are expected to account for 47 percent in 2016. Emerging economies will be the primary drivers of credit card revenue. Brazil and China, growing at 14 percent and 29 percent CAGR respectively, will account for 50
percent of total global growth. Argentina, India and Indonesia will also experience high growth in credit card revenue. Australia, Canada and the United States will continue to grow as well, albeit at a much slower pace than the emerging markets.

Issues and Challenges in the Credit Card Industry:
The Credit card industry has been growing at a very fast pace everywhere. But in their race they are forgetting that they are giving rise to defaults and manipulations all together. The use of Credit cards has changed the consumer behavior extensively. Nowadays a credit card has become a fashion orientation symbol. People are now more inclined towards impulsive buying than being frugal. They are buying blindly; they are buying things which are of little use to them and they are also buying beyond their paying capacity just because of the fact that with credit cards they can delay their payments.

The bad practices and increased cases of cloning of credit cards are on a rise as people want to defer their payments and sometimes want to evade them. People are using credit cards more as a borrowing tool than as a payment mechanism. This sudden rush in borrowing has prompted concerns that consumer debt may spiral out of control, especially in China, Thailand and South Korea. In South Korea, household debt grew 20.3 percent in 2001. In Thailand, the National Economic and Social Development Board has warned that the rapid growth in consumer lending, particularly through the use of credit cards, could jeopardize the country’s future economic stability.

Credit-card fraud is a problem that exclusively concerns emerging card markets. According to a report, the number of consumers who tend to use credit card beyond their paying ability is increasing. With over 100 million credit cards issued to the public around the end of 2002, consumer bankruptcies have erupted in recent years and there are grave concerns that the number will significantly increase as credit card debts mount up and distress more consumers financially. Deregulation by emerging-markets governments and simplification of the credit-card application process have resulted in consumers taking advantage of the new lines of credit open to them, borrowing up to their full credit.

One of the other challenges credit card issuers face is generating a sufficient volume of profitable accounts while, at the same time, being selective in granting accounts and credit lines to maintain an acceptable level of credit risk. The issuing bank manages these risks by issuing cards only to those with a risk profile it is comfortable with and then setting reasonable account limits. Banks are more likely to issue credit cards to relatively high-income individuals as there is greater likelihood that they will promptly repay their debts and have low default rates, besides having greater prospects of extensive card use.

In a bid to lure customers, credit card companies have started unethical practices, in the absence of any regulatory framework. Most credit card-issuing banks, in violation of the spirit of basic banking principles, have been sending unsolicited cards to customers. Many customers are billed for cards lost in transit and unauthorized used by someone else. Moreover, propriety demands that additional cards be issued only on the request of customers and not otherwise. Many credit card issuers levy charges without seeking the consent of customers. For instance, Citibank, the largest issuer of credit cards in India, has unilaterally levying a host of charges like Suraksha.
Credit Shield Premia, transaction Handling Charge and Suraksha Personal Accident Premia.

**Future Trend of Global Credit Cards:**
During and immediately after the financial crisis, credit card issuers tightened up lending standards and lowered credit limits to protect themselves. The bankers had given credit to too many people and approved people that had too low a credit score. So many of those people defaulted on their credit cards, and issuers were forced to eat that balance. That has been gradually changing, and experts predict more changes on the horizon for credit card holders next year.

- **Varied Rewards Redemption Choices:** These are being offered in addition to the traditional credit card rewards that are redeemable for travel, cash or gift cards. The credit card issuers are getting more creative, a trend that will likely continue in future. The reward programs are getting more competitive and offering out-of-the-box things like experiential rewards or redemption directly through retailers like Amazon.com.

- **Creative Perks:** A few credit card issuers began offering cardholders extra perks such as free Amazon Prime and Trip It Pro memberships, or credit scores included at no charge on each credit card statement. The issuers compete for market share, and credit card companies will give something else in addition to sign-up bonuses. Also on the cards are more partnerships between retailers and credit card issuers, such as concert or sports tickets available to holders of certain cards or special incentives for using a card at a certain retailer.

- **Mobile Payment Opportunities:** Mobile apps that allow consumers to check their accounts on the pay by scanning their phone at a checkout will continue to change the payment landscape in future. The most that smartphone owners now just want is to check balances, rewards and so on. Google Wallet, Square, PayPal and others are to keep innovating to take business away from the traditional credit card issuers. Much of the move toward mobile payments is driven by consumer demand for convenience. A new product called Coin is expected to hit the consumer market next summer and will store multiple credit cards and debit cards on a single device to de-clutter wallets.

- **Chip and PIN Cards:** Chip and PIN cards (also called EMV which stands for its original developers: Europay, MasterCard and Visa) have been the standard in Europe since the mid-2000’s and have stymied some Americans trying to use magnetic strip credit cards abroad. Instead of using a magnetic strip to contact a bank’s servers for authorization, EMV cards have a tiny chip that stores information like the consumer’s credit limit and card’s expiry date. Although EMV cards are more secure than magnetic strip cards, only a few U.S. card issuers offered them until recently.

- **Options for Consumers with Bad Credit:** In recent years, the most generous credit card rewards, interest-free introductory periods and creative perks have been available to cardholders with excellent credit. But as the economy improves or stays the same, issuers need to increase market share. They will typically start to loosen credit standards ever so slightly to appeal to more and more consumers. However, the introductory offers available to these consumers may be less generous than those heavily marketed offers given to consumers with strong credit scores.
Conclusion:
The credit card companies have expanded quickly into the global market in order to exploit the opportunities that are provided by the emerging economies. Emerging economies will be the primary drivers of credit card revenue. Brazil and China, growing at 14 percent and 29 percent CAGR respectively, will account for 50 percent of total global growth. Argentina, India and Indonesia will also experience high growth in credit card revenue. Australia, Canada and the United States will continue to grow as well, albeit at a much slower pace than the emerging markets. The consumer credit card market is reaching the saturation point, so the industry needs to develop marketing strategies that appeal to changing customer needs in order to encourage credit card usage.

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